S. 758. A bill to amend the Internal Revenue Code of 1986 to provide for S corporation reform, and for other purposes; to the Committee on Finance.

By Mr. BRADLEY (for himself and Mr. HOLLINGS):

S. 759. A bill to amend the Immigration and Nationality Act to limit the adjustment of status of aliens who are unlawfully residing in the United States; to the Committee on the Judiciary.

By Mr. ROCKEFELLER:

S. 760. A bill to establish the National Commission on the Long-Term Solvency of the Medicare Program; to the Committee on Finance.

SUBMISSION OF CONCURRENT AND SENATE RESOLUTIONS

The following concurrent resolutions and Senate resolutions were read, and referred (or acted upon), as indicated:

By Mrs. MURRAY:

S. Con. Res. 12. A concurrent resolution expressing the sense of the Congress concerning the trafficking of Burmese women and girls into Thailand for the purposes of forced prostitution; to the Committee on Foreign Relations.

STATEMENTS ON INTRODUCED BILLS AND JOINT RESOLUTIONS

By Mr. LAUTENBERG (for himself, Mrs. FEINSTEIN, Mr. SIMON and Mr. LEVIN):

S. 757. A bill to amend title 10, United States Code, to terminate the Civilian Marksmanship Program; to rescind funding for the National Board for the Promotion of Rifle Practice; and for other purposes; to the Committee on Armed Services.

THE CIVILIAN MARKSMANSHIP PROGRAM TERMINATION ACT OF 1995

Mr. LAUTENBERG. Mr. President, this morning I rise to introduce a bill to terminate a program that I think has long outlived its usefulness. It is called the Army Civilian Marksmanship Program.

It is no secret that I do not like this program. In fact, I offered an amendment to terminate it in the last Congress. It got 30 votes. The arguments then may not have been persuasive. But perhaps recent events will change that.

Like everyone else, I read the reports that come out about the terrorist bombing in Oklahoma City. And they are shocked by the scope of that tragedy. Every day we hear more and more news about confirmed dead and the fact that the search may in fact have to be abandoned. It is a tragedy that will live on forever in the minds of our democratic society and throughout the world.

But in one of these stories, Mr. President, I found information that members of extremist militia groups in this country may have received weapons, ammunition, and training at Army facilities under the auspices of the Civilian Marksmanship Program.

Indeed, Mark Koerneke, the leader of the Michigan-based militia group, told ABC's ''Prime Time Live'' that he had access to U.S. military bases in Michigan for the purpose of training through this program.

We all know that one of the individuals accused of masterminding the Oklahoma City bombing, Timothy McVeigh, was associated with the Michigan-based militia group. I do not know, Mr. President, whether Timothy McVeigh received training and ammunition under the Civilian Marksmanship Program. But I know it is possible that he did.

A few days ago, Mr. President, I wrote to Secretary Perry and urged him to conduct an investigation to determine the veracity of the reports linking members of extremist militia groups to the Civilian Marksmanship Program. I also called on the Pentagon to immediately suspend the Civilian Marksmanship Program and propose terminating it in the long run.

I ask unanimous consent that a copy of the letter I sent to Secretary Perry, along with a press report related to Mark Koerneke's comments, be inserted in the RECORD.

There being no objection, the material was ordered to be printed in the RECORD, as follows:

EXHIBIT 1

U.S. SENATE,
Washington, DC, May 2, 1995.

Hon. WILLIAM J. PERRY,
Secretary of Defense,
The Pentagon,
Washington, DC.

DEAR SECRETARY PERRY: Recent press reports indicate that members of extremist militia groups in this country may have received weapons, ammunition, and training at Army facilities under the auspices of the Civilian Marksmanship Program (CMP). I am writing to urge you to conduct an investigation to determine the veracity of these reports and to ask that you provide me with a list of all the clubs that participate in the CMP program. In the interim, I urge you to immediately suspend the CMP and propose terminating it in the long run.

As you know, I have long believed the CMP is a low priority program and is an egregious example of waste in government. The program promotes rifle training for civilians through a system of affiliated clubs and other organizations, and sponsors shooting competitions. As part of these activities, the program donates, loans, and sells weapons, ammunition and other shooting supplies.

The program was first established in 1903, at a time when civilian marksmanship training was believed to be important for military preparedness. Yet, according to a report by the General Accounting Office, the program now has limited military value. As Army officials told the GAO, no Army requirements exist for civilians trained in marksmanship, and no system is in place to track program-trained personnel. In a March 15, 1994 hearing in the Senate Defense Appropriations Subcommittee, Army Secretary West stated that national security objectives will be met with or without the CMP.

In essence, the CMP provides a taxpayer subsidy for recreational shooting. In light of budget deficit we face and the military needs we ought to address, this simply is not a justifiable use of scarce resources. After all, defense dollars are not used to subsidize other sports. They ought not to be used to subsidize a shooting program which has no relationship to military needs and requirements.

At a minimum we ought to ensure the CMP is not being used to train and arm members of extremist militia groups. The American people have a right to know that their tax dollars are not being used to train people who pose a threat to law abiding citizens and to peace and order in this country.

I appreciate your prompt attention to this request.

Sincerely,

FRANK P. LAUTENBERG.

U.S. RIFLERY PROGRAM MAY AID MILITIAS

(By Colum Lynch)

NEW YORK.—Even as the Clinton administration moves to monitor extremist groups that hate federal agencies, the government continues to fund a $2.5 million program that may have provided elements of such groups with low-cost surplus weapons, free bullets and access to Army training facilities.

Mark Koernke, the shortwave radio broadcaster and leader of the Michigan Militia group that disdains the federal government, suggested the embarrassing prospect that the government was aiding some of its domestic adversaries when he told ABC's ''Prime Time Live'' Tuesday that he had gained access to US military bases in Michigan to train through the 92-year-old Civilian Marksmanship Program.

Critics of the federal program, which provides about 1,150 civilian gun clubs around the country with access to military firing ranges and more than 40 million rounds of free ammunition, are demanding that the Pentagon immediately suspend the financing and launch an investigation into whether the program has provided training facilities and equipment to Koernke and to antigovernment militia groups.

Investigators also want to probe for possible links to Oklahoma City bombing suspect Timothy McVeigh, and brothers James and Terry Nichols, who allegedly helped McVeigh produce explosives in recent years.

''Our government may be inadvertently arming and training individuals and groups whose goal is to harm law enforcement officials and other innocent people,'' said Rep. Carolyn Maloney, a New York Democrat who has led an unsuccessful two-year battle in Congress to halt the program.

To be sure, many thousands of law-abiding gun enthusiasts have used the program over the years to hone their skills with no other goal than to operate their weapons safely, effectively and peacefully. In Michigan alone, there are 51 clubs with more than 6,400 members in the riflery program.

Army officials yesterday defended the program as a valuable public service, particularly useful in training youths to handle weapons. Still, the Pentagon last year suggested the program might have outlived its usefulness.

The program was started in 1903. Military officials during the Spanish-American War were appalled at the ineptitude of American marksmanship and sought to remedy that by providing rifle training to civilians in peacetime.

''It was discovered that the majority of Americans who were recruited to fight in that war couldn't hit the side of a barn,'' said Martha Rudd, an Army spokeswoman in Virginia. ''The program has been continued ever since. And the only way that it can be made to go away is if Congress makes it go away.''

In addition to providing civilian marksmen with access to military facilities, the Army also sells up to 6,000 surplus M–1 rifles annually to club participants at a bargain cost of $250 apiece. Each year, the program funds what one Army official called ''the World Series of marksmanship,'' a shooting tournament at Camp Perry, Ohio, hosted by the Army and the National Rifle Association.

Army officials said yesterday that the riflery program is an innocent recreational affair that promotes civic virtue and in particular aids the safe training of youths ages 10 to 18. In the 1980s, Rudd said, the military worked to discourage more extreme militia organizations from participating by insisting that each club chapter include at least 10 youths.

But she said that adults are welcome to participate and that it is impossible to say whether Koernke or other groups hostile to the government received ammunition or purchased weapons through the program.

In a letter to Defense Secretary William J. Perry, Maloney requested a list of the gun clubs and military bases participating, as well as information on ''links between this program and militia groups or individual extremists.'' Rudd said no investigation into the program had been initiated.

Maloney also circulated a bill calling on Congress to end the program.

''Long before this bombing, the Civilian Marksmanship Program stood out as one of the most ridiculous items in the federal government budget,'' she said. ''We're slashing funding for abused children, foster care and child nutrition, yet we're subsidizing recreational marksmanship.''

Indeed, the Pentagon issued a report to Congress last year that said the program no longer served a military purpose. Even conservative commentator George Will has referred to it as ''petrified pork.'' However, largely because of lobbying by the NRA and resistance from some Democratic and Republican supporters, the program has survived.

''The NRA has been the official agent for the Civilian Marksmanship Program,'' contended Bob Walker, the legislative director for Handgun Control Inc., a Washington-based group advocating gun control. ''In order to qualify for surplus rifles and free ammunition, one of the requirements is that you belong to the NRA. This program is a subsidy for the NRA and its members.''

The NRA press office did not respond yesterday to several requests for an interview.

Mr. LAUTENBERG. Mr. President, I have long believed the Civilian Marksmanship Program is a low priority program and an egregious example of waste in government. The program promotes rifle training for civilians through a system of affiliated clubs and other organizations, and sponsors shooting competitions. As part of these activities, the program donates, loans, and sells weapons, ammunition, and other shooting supplies.

The program was first established in 1903, soon after the Spanish-American War, at a time when civilian marksmanship training was believed to be important for military preparedness. Back then, some Federal officials were concerned that recruits often were unable to shoot straight. The officials believed that a trained corps of civilians with marksmanship skills would be useful to prepare for future military conflicts.

Mr. President, that may have made sense in 1903. But this is 1995. The Spanish-American War ended more than 90 years ago, and things have changed.

According to a report by the General Accounting Office, the program now has limited military value. As Army officials told the GAO, no Army requirements exist for civilians trained in marksmanship. In a March 15, 1994, hearing in the Senate Defense Appropriations Subcommittee, Army Secretary West stated that national security objectives will be met with or without the Civilian Marksmanship Program.

Unlike the situation in 1903 and the Spanish-American War, today we have well-trained Reserves and National Guard Forces, and we have advanced, high-technology weapons systems. The military does not need a ready supply of ordinary civilians who know how to shoot a rifle.

Even if we did need such a corps, the program does not give us one. No system is in place that tracks the program-trained personnel, and the program is not part of the Army plan for mobilizing forces in an emergency.

In essence, the Civilian Marksmanship Program provides a taxpayer subsidy for recreational shooting. In light of the budget deficit we face and the military needs we ought to address, this simply is not a justifiable use of scarce resources.

After all, defense dollars are not used to subsidize other sports. They ought not be used to subsidize a shooting program which has no relationship to military needs and requirements. Training young people to play baseball is a nice thing to do, but the Government does not subsidize Little League. We do not give children free baseballs? Why should we give them bullets?

Mr. President, Americans are deeply cynical about the Congress. They think we are controlled by narrow special interests and that we are wasting taxpayers' money on useless boondoggles. A program like bucks for bullets only reinforces that image.

It also makes people wonder about our priorities. After all, how can we close military bases and lay off thousands of defense workers while spending money on recreational gun clubs? How can we fail to fully fund Head Start if we can pass out free bullets to school kids? How can we omit funds for people unable to afford a college education if we can find millions to teach kids how to shoot?

Where is our sense of priorities? Where is our common sense?

Mr. President, I hope my colleagues will agree that it is time to end this program. At a minimum, Mr. President, we ought to ensure the Civilian Marksmanship Program is not being used to train and arm members of extremist militia groups. The American people have a right to know that their tax dollars are not being used to train people who pose a threat to law-abiding citizens and to peace and order in this country.

I urge my colleagues to cosponsor this bill, and I ask unanimous consent that a copy of the bill be printed in the RECORD.

There being no objection, the bill was ordered to be printed in the RECORD, as follows:

S. 757

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. TERMINATION OF THE CIVILIAN MARKSMANSHIP PROGRAM.

Chapter 410 of title 10, United States Code, is amended—

(1) by striking out sections 4307, 4308, 4310, 4311, 4312, and 4313;

(2) in section 4309—

(A) in subsection (a), by striking out ''and by persons capable of bearing arms'' and inserting in lieu thereof ''law enforcement agencies''; and

(B) in subsection (b), by striking out ''civilians'' each place it appears in paragraphs (1) and (3) and inserting in lieu thereof ''law enforcement agencies''; and

(3) in the table of sections at the beginning of chapter 410 of such title, by striking out the items relating to sections 4307, 4308, 4310, 4311, 4312, and 4313.

SEC. 2. RESCISSION OF FUNDS FOR NATIONAL BOARD FOR THE PROMOTION OF RIFLE PRACTICE.

The unobligated balanced of the funds appropriated by title II of Public Law 103–335 under the heading ''NATIONAL BOARD FOR THE PROMOTION OF RIFLE PRACTICE, ARMY'' is rescinded.

SEC. 3. FISCAL YEAR 1996 FUNDING NOT AUTHORIZED FOR THE NATIONAL BOARD FOR THE PROMOTION OF RIFLE PRACTICE.

Funds are not authorized to be appropriated for the National Board for the Promotion of Rifle Practice.

Mrs. FEINSTEIN. Mr. President, I rise in support of the Senator from New Jersey in this legislation to rescind the appropriation for the Civilian Marksmanship Program. I do so for a number of reasons, and I want to briefly cite them.

At a time when our Government and this body is cutting virtually every program that benefits people all across the board, I think the Civilian Marksmanship Program is one program that is truly expendable and can be rescinded. As was pointed out, the military has said this program is not necessary. The General Accounting Office in 1990 found the program unnecessary and not related to the military mission.

In March 1994, the Department of Defense testified before the Defense Subcommittee on Appropriations that the Civilian Marksmanship Program was not related to our Nation's military readiness and had no effect on our national security objectives.

About a week ago, Mr. President, I had a group gathered of major law enforcement organizations to talk about the intended repeal of the assault weapons legislation, and the head of a Federal law enforcement organization handed me a copy of the National Rifle Association's letter, a 6-page direct-mail piece that went out, and said to me this was received by one of our law enforcement people who was, frankly, amazed that this kind of rhetoric could appear on an NRA direct-mail piece.

I took a look at it, and I was astonished by what I saw. Since that time, a number of Members of the Senate have commented in the Chamber on their concern about this piece. It was

thought that the National Rifle Association might agree that it was hyper hyperbole and that it seemed to have a purpose to incite people to take action against the Federal Government, and it made statements which were in effect libelous; they were untrue; they were slanderous; statements like it did not matter to those of us who support the assault weapons ban that it gave ''jack-booted Government thugs more power to take away our constitutional rights, break in our doors, seize our guns, destroy our property, and even injure or kill us.''

Mr. President, I have had a lot of things said about me but never that. That is untrue. It is a lie. It is patently false and it is said for one reason and one reason only, and that is to incite people.

Then it goes on to say, ''President Clinton's army of antigun Government agents continue to intimidate and harass law-abiding citizens. In Clinton's administration, if you have a badge, you have the Government's go ahead to harass, to intimidate, and to even murder law-abiding citizens.''

On its face, that is slanderous and in writing it is libelous. It is factually untrue. It is said but for one reason and one reason only. And that is to incite and develop hatred against the Federal Government and the very people who carry out the intent of the laws that we in this body and the other body pass and are signed by the President and become the law of the land. I do not think this body can condone this kind of rhetoric.

Now, is this connected with the Civilian Marksmanship Program? Not directly. Not directly. But indirectly it is, because the NRA effectively participates in this program—it is estimated by some to the extent of $1 million out of the $2.5 million appropriation.

Moreover, given the association's refusal to recant this letter, a letter which is blatantly political and inciting, certainly not one of a nonpolitical organization, should Federal funds benefit a political organization of this type? I would come down and say no, Federal moneys should not go to benefit an organization that openly admits it plays a major political role in the election and in the unelection of Members of Congress and members of other local bodies.

I believe letters of this kind really defeat its purpose as a so-called nonpolitical organization.

In addition, I am disturbed about recent reports, such as the ABC ''PrimeTime Live'' episode and a Boston Globe article, that describe how militia members brag that they have received ammunition, surplus weaponry, and training on Army bases through the Civilian Marksmanship Program.

I do not know whether this is true or not. I have no way on my own of verifying it, but the fact is they did brag that this was the case.

In fact, my staff was recently told by the Department of Defense about a recent incident where a military security patrol monitoring an Army rifle range saw that club members were using the range and wearing Michigan militia patches. These club members were asked to leave the range, which is located at Camp Grayling, MI, on April 27.

As DOD staff admit, there is nothing in the regulations of this program to prevent militia members from joining civilian marksmanship clubs and receiving ammunition, weaponry, and access to military training facilities, because—and I stress this—the program does not check members for their membership in other organizations or limit the number of adults that can join.

So in light of these reports, which suggest this possibility to train, supply, or subsidize anti-Government extremist militias, and the letter which seems to indicate to me, and I think to other reasonable readers of the letter, that the National Rifle Association is willing to go a step further to raise the level of the rhetoric, to increase the hostility, one can certainly question the wisdom of Federal dollars going to provide weapons and bullets and training to groups who may—and I say may and I say might—use these weapons and use that training against the very people that this body empowers to carry out our laws.

So I believe the time has come to take definitive, direct action and, by that action, to send a message that we will not, in fact, tolerate this. That is why I am cosponsoring this legislation, and I hope this body will be receptive to its passage.

By Mr. HATCH (for himself, Mr. PRYOR, Mr. SIMPSON, Mr. BREAUX, Mr. LUGAR, Mr. LEAHY, Mrs. HUTCHISON, Mrs. MURRAY, Mr. BOND, Mr. KEMPTHORNE, Mr. JOHNSTON, Mr. FORD, Mr. ROBB, Mr. DORGAN, Mr. KERREY, Mr. KYL, Mr. BAUCUS, Mr. CRAIG, Mr. COCHRAN, Mr. COHEN, Mr. GRASSLEY, Mr. D'AMATO, Mr. BENNETT, and Mr. BINGAMAN):

S. 758. A bill to amend the Internal Revenue Code of 1986 to provide for S corporation reform, and for other purposes; to the Committee on Finance.

THE S CORPORATION REFORM ACT OF 1995

Mr. HATCH. Mr. President, on behalf of myself and Senator PRYOR, I rise today to introduce the S Corporation Reform Act of 1995. We are pleased to be joined by Senators SIMPSON, BREAUX, LUGAR, LEAHY, HUTCHISON, MURRAY, BOND, KEMPTHORNE, JOHNSTON, FORD, ROBB, DORGAN, KERREY of Nebraska, KYL, BAUCUS, CRAIG, COCHRAN, GRASSLEY, D'AMATO, COHEN, BENNETT, and BINGAMAN.

Mr. President, today almost 1.7 million businesses pay taxes as S corporations and the vast majority of these are small enterprises. As we all know, small business is the engine that drives American job creation. It is important to note that while in ordinary times, small businesses create half of the new jobs in this country, in times of recovery, this number jumps to 75 percent. It is obvious that the tax and economic policies of this Nation should support and sustain the creation and growth of small businesses. Our economic future depends on the health and strength of our small business sector.

This is why we are introducing a bill today to strengthen small businesses.

Mr. President, this bill will help to fine-tune the Nation's job-creating engine of small business in three ways: by improving access to capital, by making it easier to pass on family-owned businesses from one generation to the next, and by simplifying many of the outdated, unnecessary and complex tax rules that apply to S corporations.

One of the biggest problems facing small business is that of attracting adequate capital. This bill helps to expand access to capital by S corporations by increasing the number of permitted shareholders from 35 to 50, by permitting tax-exempt organizations to be shareholders, and by allowing non-citizens to own S corporation stock. It will also modernize S corporation financing by allowing them to issue preferred stock and convertible bonds.

Further, this legislation will make it easier for one S corporation to own another corporation. Our outmoded rules already permit this, but not without a sizeable diversion of capital away from productive investment and into the pockets of lawyers and accountants. This bill's provisions will streamline small business structure and return common sense to the realm of business ownership.

Additionally, the bill will help preserve family-owned businesses by making it easier for families to establish trusts funded by S corporation shares, and by counting all members of a family who hold S corporation stock as a single shareholder. These are important provisions, Mr. President, because so many successful small businesses fail to survive beyond the first generation.

Finally, the bill will repair a number of outmoded, inefficient provisions of S corporation tax law. Among the revised rules are a provision giving fringe benefits in S corporations the same tax treatment provided to ordinary corporations, and another which will stop corporate elections from being invalidated by mere technicalities. Most importantly, all of the bill's provisions have been carefully designed to avoid creating future difficulties for America's small businesses.

In my home state of Utah, there are thousands of current and future entrepreneurs for whom this bill will provide much-needed financial and legal flexibility in the increasingly competitive marketplace. Throughout the country, small businessmen and women have

been clamoring for relief from our Nation's outdated and inflexible policies regarding S corporation.

I encourage my colleagues to support this badly needed legislation, which will give small businesses the strength and flexibility they will need to thrive into the next century.

Mr. President, there is much talk these days about tax simplification and about throwing out the old tax system and starting over again with a better one that makes more sense. This debate is a very positive thing for this country and I believe it will eventually lead to some vast improvements in the way our economy operates. In the meantime, however, let us not overlook some of the relatively simple and noncontroversial changes that will make our tax system work better. This bill represents such changes. These are improvements that we can make right now that will help small and growing businesses.

I ask unanimous consent that the text of this bill be printed in the RECORD.

There being no objection, the bill was ordered to be printed in the RECORD, as follows:

S. 758

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE; AMENDMENT OF 1986 CODE; TABLE OF CONTENTS.

(a) SHORT TITLE.—This Act may be cited as the ''S Corporation Reform Act of 1995''.

(b) AMENDMENT OF 1986 CODE.—Except as otherwise expressly provided, whenever in this Act an amendment or repeal is expressed in terms of an amendment to, or repeal of, a section or other provision, the reference shall be considered to be made to a section or other provision of the Internal Revenue Code of 1986.

(c) TABLE OF CONTENTS.—The table of contents is as follows:

TITLE I—ELIGIBLE SHAREHOLDERS OF S CORPORATION

Subtitle A—Number of Shareholders

SEC. 101. S CORPORATIONS PERMITTED TO HAVE 50 SHAREHOLDERS.

Subparagraph (A) of section 1361(b)(1) (defining small business corporation) is amended by striking ''35 shareholders'' and inserting ''50 shareholders''.

SEC. 102. MEMBERS OF FAMILY TREATED AS 1 SHAREHOLDER.

Paragraph (1) of section 1361(c) (relating to special rules for applying subsection (b)) is amended to read as follows:

''(1) MEMBERS OF FAMILY TREATED AS 1 SHAREHOLDER.—

''(A) IN GENERAL.—For purposes of subsection (b)(1)(A)—

''(i) except as provided in clause (ii), a husband and wife (and their estates) shall be treated as 1 shareholder, and

''(ii) in the case of a family with respect to which an election is in effect under subparagraph (E), all members of the family shall be treated as 1 shareholder.

''(B) MEMBERS OF THE FAMILY.—For purposes of subparagraph (A)(ii), the term 'members of the family' means the lineal descendants of the common ancestor and the spouses (or former spouses) of such lineal descendants or common ancestor.

''(C) COMMON ANCESTOR.—For purposes of this paragraph, an individual shall not be considered a common ancestor if, as of the later of the effective date of this paragraph or the time the election under section 1362(a) is made, the individual is more than 6 generations removed from the youngest generation of shareholders.

''(D) EFFECT OF ADOPTION, ETC.—In determining whether any relationship specified in subparagraph (B) or (C) exists, the rules of section 152(b)(2) shall apply.

''(E) ELECTION.—An election under subparagraph (A)(ii)—

''(i) must be made with the consent of all shareholders,

''(ii) shall remain in effect until terminated, and

''(iii) shall apply only with respect to 1 family in any corporation.''.

Subtitle B—Persons Allowed as Shareholders

SEC. 111. CERTAIN EXEMPT ORGANIZATIONS.

(a) CERTAIN EXEMPT ORGANIZATIONS ALLOWED TO BE SHAREHOLDERS.—

(1) IN GENERAL.—Subparagraph (B) of section 1361(b)(1) (defining small business corporation) is amended to read as follows:

''(B) have as a shareholder a person (other than an estate, a trust described in subsection (c)(2), or an organization described in subsection (c)(7)) who is not an individual,''.

(2) ELIGIBLE EXEMPT ORGANIZATIONS.—Section 1361(c) (relating to special rules for applying subsection (b)) is amended by adding at the end the following new paragraph:

''(7) CERTAIN EXEMPT ORGANIZATIONS PERMITTED AS SHAREHOLDERS.—For purposes of subsection (b)(1)(B), an organization described in section 401(a) or 501(c)(3) may be a shareholder in an S corporation.''

(b) CONTRIBUTIONS OF S CORPORATION STOCK.—Section 170(e)(1) (relating to certain contributions of ordinary income and capital gain property) is amended by adding at the end the following sentence: ''For purposes of applying this paragraph in the case of a charitable contribution of stock in an S corporation, rules similar to the rules of section 751 shall apply in determining whether gain on such stock would have been long-term capital gain if such stock were sold by the taxpayer.''

(c) SPECIAL RULES APPLICABLE TO PARTNERSHIPS AND S CORPORATIONS.—

(1) IN GENERAL.—Subsection (c) of section 512 (relating to unrelated business tax income) is amended—

(A) by inserting ''or S corporation'' after ''partnership'' each place it appears in paragraphs (1) and (3),

(B) by inserting ''or shareholder'' after ''member'' in paragraph (1), and

(C) by inserting ''AND S CORPORATIONS'' after ''PARTNERSHIPS'' in the heading.

(2) REPORTING REQUIREMENT.—Section 6037 (relating to return of S corporation) is amended by adding at the end the following new subsection:

''(c) SEPARATE STATEMENT OF ITEMS OF UNRELATED BUSINESS TAXABLE INCOME.—In the case of any S corporation regularly carrying on a trade or business (within the meaning of section 512(c)(1)), the information required under subsection (b) to be furnished to any shareholder described in section 1361(c)(7) shall include such information as is necessary to enable the shareholder to compute its pro rata share of the corporation's income or loss from the trade or business in accordance with section 512(a)(1), but without regard to the modifications described in paragraphs (8) through (15) of section 512(b).''

SEC. 112. FINANCIAL INSTITUTIONS.

Subparagraph (B) of section 1361(b)(2) (defining ineligible corporation) is amended to read as follows:

''(B) a financial institution which uses the reserve method of accounting for bad debts described in section 585 or 593,''.

SEC. 113. NONRESIDENT ALIENS.

(a) NONRESIDENT ALIENS ALLOWED TO BE SHAREHOLDERS.—

(1) IN GENERAL.—Paragraph (1) of section 1361(b) (defining small business corporation) is amended—

(A) by adding ''and'' at the end of subparagraph (B),

(B) by striking subparagraph (C), and

(C) by redesignating subparagraph (D) as subparagraph (C).

(2) CONFORMING AMENDMENTS.—Paragraphs (4) and (5)(A) of section 1361(c) (relating to special rules for applying subsection (b)) are each amended by striking ''subsection (b)(1)(D)'' and inserting ''subsection (b)(1)(C)''.

(b) NONRESIDENT ALIEN SHAREHOLDER TREATED AS ENGAGED IN TRADE OR BUSINESS WITHIN UNITED STATES.—

(1) IN GENERAL.—Section 875 is amended—

(A) by striking ''and'' at the end of paragraph (1),

(B) by striking the period at the end of paragraph (2) and inserting '', and'', and

(C) by adding at the end the following new paragraph:

''(3) a nonresident alien individual shall be considered as being engaged in a trade or business within the United States if the S corporation of which such individual is a shareholder is so engaged.''

(2) APPLICATION OF WITHHOLDING TAX ON NONRESIDENT ALIEN SHAREHOLDERS.—Section 1446 (relating to withholding tax on foreign partners' share of effectively connected income) is amended by redesignating subsection (f) as subsection (g) and by inserting after subsection (e) the following new subsection:

''(f) S CORPORATION TREATED AS PARTNERSHIP, ETC.—For purposes of this section—

''(1) an S corporation shall be treated as a partnership,

''(2) the shareholders of such corporation shall be treated as partners of such partnership, and

''(3) any reference to section 704 shall be treated as a reference to section 1366.''

(3) CONFORMING AMENDMENTS.—

(A) The heading of section 875 is amended to read as follows:

"SEC. 875. PARTNERSHIPS; BENEFICIARIES OF ESTATES AND TRUSTS; S CORPORATIONS."

(B) The heading of section 1446 is amended to read as follows:

"SEC. 1446. WITHHOLDING TAX ON FOREIGN PARTNERS' AND S CORPORATE SHAREHOLDERS' SHARE OF EFFECTIVELY CONNECTED INCOME."

(4) CLERICAL AMENDMENTS.—

(A) The item relating to section 875 in the table of sections for subpart A of part II of subchapter N of chapter 1 is amended to read as follows:

''Sec. 875. Partnerships; beneficiaries of estates and trusts; S corporations.''

(B) The item relating to section 1446 in the table of sections for subchapter A of chapter 3 is amended to read as follows:

''Sec. 1446. Withholding tax on foreign partners' and S corporate shareholders' share of effectively connected income.''

(c) PERMANENT ESTABLISHMENT OF PARTNERS AND S CORPORATION SHAREHOLDERS.—Section 894 (relating to income affected by treaty) is amended by adding at the end the following new subsection:

''(c) PERMANENT ESTABLISHMENT OF PARTNERS AND S CORPORATION SHAREHOLDERS.—If a partnership or S corporation has a permanent establishment in the United States (within the meaning of a treaty to which the United States is a party) at any time during a taxable year of such entity, a nonresident alien individual or foreign corporation which is a partner in such partnership, or a nonresident alien individual who is a shareholder in such S corporation, shall be treated as having a permanent establishment in the United States for purposes of such treaty.''

SEC. 113. ELECTING SMALL BUSINESS TRUSTS.

(a) GENERAL RULE.—Subparagraph (A) of section 1361(c)(2) (relating to certain trusts permitted as shareholders) is amended by inserting after clause (iv) the following new clause:

''(v) An electing small business trust.''

(b) CURRENT BENEFICIARIES TREATED AS SHAREHOLDERS.—Subparagraph (B) of section 1361(c)(2) is amended by adding at the end the following new clause:

''(v) In the case of a trust described in clause (v) of subparagraph (A), each potential current beneficiary of such trust shall be treated as a shareholder; except that, if for any period there is no potential current beneficiary of such trust, such trust shall be treated as the shareholder during such period.''

(c) ELECTING SMALL BUSINESS TRUST DEFINED.—Section 1361 (defining S corporation) is amended by adding at the end the following new subsection:

''(e) ELECTING SMALL BUSINESS TRUST DEFINED.—

''(1) ELECTING SMALL BUSINESS TRUST.—For purposes of this section—

''(A) IN GENERAL.—Except as provided in subparagraph (B), the term 'electing small business trust' means any trust if—

''(i) such trust does not have as a beneficiary any person other than an individual, an estate, or an organization described in section 401(a) or 501(c)(3),

''(ii) no interest in such trust was acquired by purchase, and

''(iii) an election under this subsection applies to such trust.

''(B) CERTAIN TRUSTS NOT ELIGIBLE.—The term 'electing small business trust' shall not include—

''(i) any qualified subchapter S trust (as defined in subsection (d)(3)) if an election under subsection (d)(2) applies to any corporation the stock of which is held by such trust, and

''(ii) any trust exempt from tax under this subtitle.

''(C) PURCHASE.—For purposes of subparagraph (A), the term 'purchase' means any acquisition if the basis of the property acquired is determined under section 1012.

''(2) POTENTIAL CURRENT BENEFICIARY.—For purposes of this section, the term 'potential current beneficiary' means, with respect to any period, any person who at any time during such period is entitled to, or at the discretion of any person may receive, a distribution from the principal or income of the trust. If a trust disposes of all of the stock which it holds in an S corporation, then, with respect to such corporation, the term 'potential current beneficiary' does not include any person who first met the requirements of the preceding sentence during the 60-day period ending on the date of such disposition.

''(3) ELECTION.—An election under this subsection shall be made by the trustee in such manner and form, and at such time, as the Secretary may prescribe. Any such election shall apply to the taxable year of the trust for which made and all subsequent taxable years of such trust unless revoked with the consent of the Secretary.

''(4) CROSS REFERENCE.—

"For special treatment of electing small business trusts, see section 641(d)."

(d) TAXATION OF ELECTING SMALL BUSINESS TRUSTS.—Section 641 (relating to imposition of tax on trusts) is amended by adding at the end the following new subsection:

''(d) SPECIAL RULES FOR TAXATION OF ELECTING SMALL BUSINESS TRUSTS.—

''(1) IN GENERAL.—For purposes of this chapter—

''(A) the portion of any electing small business trust which consists of stock in 1 or more S corporations shall be treated as a separate trust, and

''(B) the amount of the tax imposed by this chapter on such separate trust shall be determined with the modifications of paragraph (2).

''(2) MODIFICATIONS.—For purposes of paragraph (1), the modifications of this paragraph are the following:

''(A) Except as provided in section 1(h), the amount of the tax imposed by section 1(e) shall be determined by using the highest rate of tax set forth in section 1(e).

''(B) The exemption amount under section 55(d) shall be zero.

''(C) The only items of income, loss, deduction, or credit to be taken into account are the following:

''(i) The items required to be taken into account under section 1366.

''(ii) Any gain or loss from the disposition of stock in an S corporation.

''(iii) To the extent provided in regulations, State or local income taxes or administrative expenses to the extent allocable to items described in clauses (i) and (ii).

No deduction or credit shall be allowed for any amount not described in this paragraph, and no item described in this paragraph shall be apportioned to any beneficiary.

''(D) No amount shall be allowed under paragraph (1) or (2) of section 1211(b).

''(3) TREATMENT OF REMAINDER OF TRUST AND DISTRIBUTIONS.—For purposes of determining—

''(A) the amount of the tax imposed by this chapter on the portion of any electing small business trust not treated as a separate trust under paragraph (1), and

''(B) the distributable net income of the entire trust,

the items referred to in paragraph (2)(C) shall be excluded. Except as provided in the preceding sentence, this subsection shall not affect the taxation of any distribution from the trust.

''(4) TREATMENT OF UNUSED DEDUCTIONS WHERE TERMINATION OF SEPARATE TRUST.—If a portion of an electing small business trust ceases to be treated as a separate trust under paragraph (1), any carryover or excess deduction of the separate trust which is referred to in section 642(h) shall be taken into account by the entire trust.

''(5) ELECTING SMALL BUSINESS TRUST.—For purposes of this subsection, the term 'electing small business trust' has the meaning given such term by section 1361(e)(1).''

Subtitle C—Other Provisions

SEC. 121. EXPANSION OF POST-DEATH QUALIFICATION FOR CERTAIN TRUSTS.

Subparagraph (A) of section 1361(c)(2) (relating to certain trusts permitted as shareholders) is amended—

(1) by striking ''60-day period'' each place it appears in clauses (ii) and (iii) and inserting ''2-year period'', and

(2) by striking the last sentence in clause (ii).

TITLE II—QUALIFICATION AND ELIGIBILITY REQUIREMENTS FOR S CORPORATIONS

Subtitle A—One Class of Stock

SEC. 201. ISSUANCE OF PREFERRED STOCK PERMITTED.

(a) IN GENERAL.—Section 1361(c), as amended by section 111(a)(2), is amended by adding at the end the following new paragraph:

''(8) TREATMENT OF QUALIFIED PREFERRED STOCK.—

''(A) IN GENERAL.—Notwithstanding subsection (b)(1)(D), an S corporation may issue qualified preferred stock.

''(B) QUALIFIED PREFERRED STOCK DEFINED.—For purposes of this paragraph, the term 'qualified preferred stock' means stock described in section 1504(a)(4) which is issued to a person eligible to hold common stock of an S corporation.

''(C) DISTRIBUTIONS.—A distribution (not in part or full payment in exchange for stock) made by the corporation with respect to qualified preferred stock shall be includible as interest income of the holder and deductible to the corporation as interest expense in computing taxable income under section 1363(b) in the year such distribution is received.''

(b) CONFORMING AMENDMENTS.—

(1) Subparagraph (C) of section 1361(b)(1), as redesignated by section 113(a)(1)(C), is

amended by inserting ''except as provided in paragraph (8),'' before ''have''.

(2) Subsection (a) of section 1366 is amended by adding at the end the following new paragraph:

''(3) ALLOCATION WITH RESPECT TO QUALIFIED PREFERRED STOCK.—The holders of qualified preferred stock shall not, with respect to such stock, be allocated any of the items described in paragraph (1).''

SEC. 202. FINANCIAL INSTITUTIONS PERMITTED TO HOLD SAFE HARBOR DEBT.

Subparagraph (B) of section 1361(c)(5) (defining straight debt) is amended by adding ''and'' at the end of clause (i) and by striking clauses (ii) and (iii) and inserting the following:

''(ii) in any case in which the terms of such promise include a provision under which the obligation to pay may be converted (directly or indirectly) into stock of the corporation, such terms, taken as a whole, are substantially the same as the terms which could have been obtained on the effective date of the promise from a person which is not a related person (within the meaning of section 465(b)(3)(C)) to the S corporation or its shareholders, and

''(iii) the creditor is—

''(I) an individual,

''(II) an estate,

''(III) a trust described in paragraph (2), or

''(IV) a person which is actively and regularly engaged in the business of lending money.''

Subtitle B—Elections and Terminations

SEC. 211. RULES RELATING TO INADVERTENT TERMINATIONS AND INVALID ELECTIONS.

(a) GENERAL RULE.—Subsection (f) of section 1362 (relating to inadvertent terminations) is amended to read as follows:

''(f) INADVERTENT INVALID ELECTIONS OR TERMINATIONS.—If—

''(1) an election under subsection (a) by any corporation—

''(A) was not effective for the taxable year for which made (determined without regard to subsection (b)(2)) by reason of a failure to meet the requirements of section 1361(b) or to obtain shareholder consents, or

''(B) was terminated under paragraph (2) of subsection (d),

''(2) the Secretary determines that the circumstances resulting in such ineffectiveness or termination were inadvertent,

''(3) no later than a reasonable period of time after discovery of the circumstances resulting in such ineffectiveness or termination, steps were taken—

''(A) so that the corporation is a small business corporation, or

''(B) to acquire the required shareholder consents, and

''(4) the corporation, and each person who was a shareholder in the corporation at any time during the period specified pursuant to this subsection, agrees to make such adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary with respect to such period,

then, notwithstanding the circumstances resulting in such ineffectiveness or termination, such corporation shall be treated as an S corporation during the period specified by the Secretary.''

(b) LATE ELECTIONS.—Subsection (b) of section 1362 is amended by adding at the end thereof the following new paragraph:

''(5) AUTHORITY TO TREAT LATE ELECTIONS AS TIMELY.—If—

''(A) an election under subsection (a) is made for any taxable year (determined without regard to paragraph (3)) after the date prescribed by this subsection for making such election for such taxable year, and

''(B) the Secretary determines that there was reasonable cause for the failure to timely make such election,

the Secretary may treat such election as timely made for such taxable year (and paragraph (3) shall not apply).''

(c) AUTOMATIC WAIVERS.—The Secretary of the Treasury shall provide for an automatic waiver procedure under section 1362(f) of the Internal Revenue Code of 1986 in cases in which the Secretary determines appropriate.

(d) EFFECTIVE DATE.—The amendments made by subsection (a) and (b) shall apply with respect to elections for taxable years beginning after December 31, 1982.

SEC. 212. AGREEMENT TO TERMINATE YEAR.

Paragraph (2) of section 1377(a) (relating to pro rata share) is amended to read as follows:

''(2) ELECTION TO TERMINATE YEAR.—

''(A) IN GENERAL.—Under regulations prescribed by the Secretary, if any shareholder terminates the shareholder's interest in the corporation during the taxable year and all affected shareholders agree to the application of this paragraph, paragraph (1) shall be applied to the affected shareholders as if the taxable year consisted of 2 taxable years the first of which ends on the date of the termination.

''(B) AFFECTED SHAREHOLDERS.—For purposes of subparagraph (A), the term 'affected shareholders' means the shareholder whose interest is terminated and all shareholders to whom such shareholder has transferred shares during the taxable year. If such shareholder has transferred shares to the corporation, the term 'affected shareholders' shall include all persons who are shareholders during the taxable year.''

SEC. 213. EXPANSION OF POST-TERMINATION TRANSITION PERIOD.

(a) IN GENERAL.—Paragraph (1) of section 1377(b) (relating to post-termination transition period) is amended by striking ''and'' at the end of subparagraph (A), by redesignating subparagraph (B) as subparagraph (C), and by inserting after subparagraph (A) the following new subparagraph:

''(B) the 120-day period beginning on the date of any determination pursuant to an audit of the taxpayer which follows the termination of the corporation's election and which adjusts a subchapter S item of income, loss, or deduction of the corporation arising during the S period (as defined in section 1368(e)(2)), and''.

(b) DETERMINATION DEFINED.—Paragraph (2) of section 1377(b) is amended by striking subparagraphs (A) and (B), by redesignating subparagraph (C) as subparagraph (B), and by inserting before subparagraph (B) (as so redesignated) the following new subparagraph:

''(A) a determination as defined in section 1313(a), or''.

(c) REPEAL OF SPECIAL AUDIT PROVISIONS FOR SUBCHAPTER S ITEMS.—

(1) GENERAL RULE.—Subchapter D of chapter 63 (relating to tax treatment of subchapter S items) is hereby repealed.

(2) CONSISTENT TREATMENT REQUIRED.—Section 6037 (relating to return of S corporation), as amended by section 111(c)(2), is amended by adding at the end the following new subsection:

''(d) SHAREHOLDER'S RETURN MUST BE CONSISTENT WITH CORPORATE RETURN OR SECRETARY NOTIFIED OF INCONSISTENCY.—

''(1) IN GENERAL.—A shareholder of an S corporation shall, on such shareholder's return, treat a subchapter S item in a manner which is consistent with the treatment of such item on the corporate return.

''(2) NOTIFICATION OF INCONSISTENT TREATMENT.—

''(A) IN GENERAL.—In the case of any subchapter S item, if—

''(i)(I) the corporation has filed a return but the shareholder's treatment on his return is (or may be) inconsistent with the treatment of the item on the corporate return, or

''(II) the corporation has not filed a return, and

''(ii) the shareholder files with the Secretary a statement identifying the inconsistency,

paragraph (1) shall not apply to such item.

''(B) SHAREHOLDER RECEIVING INCORRECT INFORMATION.—A shareholder shall be treated as having complied with clause (ii) of subparagraph (A) with respect to a subchapter S item if the shareholder—

''(i) demonstrates to the satisfaction of the Secretary that the treatment of the subchapter S item on the shareholder's return is consistent with the treatment of the item on the schedule furnished to the shareholder by the corporation, and

''(ii) elects to have this paragraph apply with respect to that item.

''(3) EFFECT OF FAILURE TO NOTIFY.—In any case—

''(A) described in subparagraph (A)(i)(I) of paragraph (2), and

''(B) in which the shareholder does not comply with subparagraph (A)(ii) of paragraph (2),

any adjustment required to make the treatment of the items by such shareholder consistent with the treatment of the items on the corporate return shall be treated as arising out of mathematical or clerical errors and assessed according to section 6213(b)(1). Paragraph (2) of section 6213(b) shall not apply to any assessment referred to in the preceding sentence.

''(4) SUBCHAPTER S ITEM.—For purposes of this subsection, the term 'subchapter S item' means any item of an S corporation to the extent that regulations prescribed by the Secretary provide that, for purposes of this subtitle, such item is more appropriately determined at the corporation level than at the shareholder level.

''(5) ADDITION TO TAX FOR FAILURE TO COMPLY WITH SECTION.—

''For addition to tax in the case of a shareholder's negligence in connection with, or disregard of, the requirements of this section, see part II of subchapter A of chapter 68.''

(3) CONFORMING AMENDMENTS.—

(A) Section 1366 is amended by striking subsection (g).

(B) Subsection (b) of section 6233 is amended to read as follows:

''(b) SIMILAR RULES IN CERTAIN CASES.—If a partnership return is filed for any taxable year but it is determined that there is no entity for such taxable year, to the extent provided in regulations, rules similar to the rules of subsection (a) shall apply.''

(C) The table of subchapters for chapter 63 is amended by striking the item relating to subchapter D.

SEC. 214. REPEAL OF EXCESSIVE PASSIVE INVESTMENT INCOME AS A TERMINATION EVENT.

(a) IN GENERAL.—Section 1362(d) (relating to termination) is amended by striking paragraph (3).

(b) MODIFICATION OF TAX IMPOSED ON EXCESSIVE PASSIVE INVESTMENT INCOME.—

(1) INCREASE IN THRESHOLD.—Subsections (a)(2) and (b)(1)(A)(i) of section 1375 (relating to tax imposed when passive investment income of corporation having subchapter C earnings and profits exceeds 25 percent of gross receipts) are each amended by striking ''25 percent'' and inserting ''50 percent''.

(2) TAX RATE INCREASE AFTER THIRD CONSECUTIVE YEAR.—Section 1375 is amended by redesignating subsections (c) and (d) as subsections (d) and (e), respectively, and by inserting after subsection (b) the following new subsection:

''(c) TAX RATE INCREASE AFTER THIRD CONSECUTIVE YEAR.—

''(1) IN GENERAL.—If an S corporation is described in subsection (a) for more than 3 consecutive taxable years, then the rate of tax imposed under subsection (a) with respect to each succeeding consecutive taxable year (if any) shall be determined under the following table:

''In the case of the—	The rate of tax imposed under subsection (a) shall be equal to such rate of tax for the 3rd taxable year, plus the following percentage points:
4th taxable year	10
5th taxable year	20
6th taxable year	30
7th taxable year	40
8th taxable year and thereafter	50.

''(2) YEARS TAKEN INTO ACCOUNT.—No tax shall be increased under paragraph (1) for any taxable year beginning before January 1, 1996.''

(c) CONFORMING AMENDMENTS.—

(1) Section 1362(f)(1) is amended by striking ''or (3)''.

(2) Subsection (b) of section 1375 is amended by striking paragraphs (3) and (4) and inserting the following new paragraphs:

''(3) SUBCHAPTER C EARNINGS AND PROFITS.—The term 'subchapter C earnings and profits' means earnings and profits of any corporation for any taxable year with respect to which an election under section 1362(a) (or under section 1372 of prior law) was not in effect.

''(4) GROSS RECEIPTS FROM SALES OF CAPITAL ASSETS (OTHER THAN STOCK AND SECURITIES).—In the case of dispositions of capital assets (other than stock and securities), gross receipts from such dispositions shall be taken into account only to the extent of the capital gain net income therefrom.

''(5) PASSIVE INVESTMENT INCOME DEFINED.—

''(A) IN GENERAL.—Except as otherwise provided in this paragraph, the term 'passive investment income' means gross receipts derived from royalties, rents, dividends, interest, and annuities.

''(B) EXCEPTION FOR INTEREST ON NOTES FROM SALES OF INVENTORY.—The term 'passive investment income' shall not include interest on any obligation acquired in the ordinary course of the corporation's trade or business from its sale of property described in section 1221(1).

''(C) TREATMENT OF CERTAIN LENDING OR FINANCE COMPANIES.—If the S corporation meets the requirements of section 542(c)(6) for the taxable year, the term 'passive investment income' shall not include gross receipts for the taxable year which are derived directly from the active and regular conduct of a lending or finance business (as defined in section 542(d)(1)).

''(D) SPECIAL RULE FOR OPTIONS AND COMMODITY DEALINGS.—

''(i) IN GENERAL.—In the case of any options dealer or commodities dealer, passive investment income shall be determined by not taking into account any gain or loss (in the normal course of the taxpayer' activity of dealing in or trading section 1256 contracts) from any section 1256 contract or property related to such a contract.

''(ii) DEFINITIONS.—For purposes of this subparagraph—

''(I) OPTIONS DEALER.—The term 'options dealer' has the meaning given such term by section 1256(g)(8).

''(II) COMMODITIES DEALER.—The term 'commodities dealer' means a person who is actively engaged in trading section 1256 contracts and is registered with a domestic board of trade which is designated as a contract market by the Commodities Futures Trading Commission.

''(III) SECTION 1256 CONTRACT.—The term 'section 1256 contract' has the meaning given to such term by section 1256(b).

''(E) COORDINATION WITH SECTION 1374.—The amount of passive investment income shall be determined by not taking into account any recognized built-in gain or loss of the S corporation for any taxable year in the recognition period. Terms used in the preceding sentence shall have the same respective meaning as when used in section 1374.''

(3) The heading for section 1375 is amended by striking ''**25**'' and inserting ''**50**''.

(4) The table of sections for part III of subchapter S of chapter 1 is amended by striking ''25'' in the item relating to section 1375 and inserting ''50''.

(5) Clause (i) of section 1042(c)(4)(A) is amended by striking ''section 1362(d)(3)(D)'' and inserting ''section 1375(b)(5)''.

Subtitle C—Other Provisions

SEC. 221. S CORPORATIONS PERMITTED TO HOLD SUBSIDIARIES.

(a) IN GENERAL.—Paragraph (2) of section 1361(b) (defining ineligible corporation), as amended by section 112, is amended by striking subparagraph (A) and by redesignating subparagraphs (B), (C), (D), and (E) as subparagraphs (A), (B), (C), and (D), respectively.

(b) TREATMENT OF CERTAIN WHOLLY OWNED S CORPORATION SUBSIDIARIES.—Section 1361(b) (defining small business corporation) is amended by adding at the end thereof the following new subsection:

''(3) TREATMENT OF CERTAIN WHOLLY OWNED SUBSIDIARIES.—

''(A) IN GENERAL.—For purposes of this title—

''(i) a corporation which is a qualified subchapter S subsidiary shall not be treated as a separate corporation, and

''(ii) all assets, liabilities, and items of income, deduction, and credit of a qualified subchapter S subsidiary shall be treated as assets, liabilities, and such items (as the case may be) of the S corporation.

''(B) QUALIFIED SUBCHAPTER S SUBSIDIARY.—For purposes of this subsection, the term 'qualified subchapter S subsidiary' means any corporation 100 percent of the stock of which is held by an S corporation as of the later of the effective date of the S election of the S corporation or the acquisition of the subsidiary, and at all times thereafter.

''(C) TREATMENT OF TERMINATIONS OF QUALIFIED SUBCHAPTER S SUBSIDIARY STATUS.—For purposes of this subtitle, if any corporation which was a qualified subchapter S subsidiary ceases to meet the requirements of subparagraph (B), such corporation shall be treated as a new corporation acquiring all of its assets (and assuming all of its liabilities) immediately before such cessation from the S corporation in exchange for its stock.''.

(c) CERTAIN DIVIDENDS NOT TREATED AS PASSIVE INVESTMENT INCOME.—Section 1375(b)(5) (defining passive investment income), as added by section 214(c)(2), is amended by adding at the end the following new subparagraph:

''(F) TREATMENT OF CERTAIN DIVIDENDS.—If an S corporation holds stock in a C corporation meeting the requirements of section 1504(a)(2), the term 'passive investment income' shall not include dividends from such C corporation to the extent such dividends are attributable to the earnings and profits of such C corporation derived from the active conduct of a trade or business.''

(d) CONFORMING AMENDMENTS.—

(1) Subsection (c) of section 1361, as amended by sections 111(a)(2) and 201(a), is amended by striking paragraph (6) and redesignating paragraphs (7) and (8) as paragraphs (6) and (7), respectively.

(2) Subsection (b) of section 1504 (defining includible corporation) is amended by adding at the end the following new paragraph:

''(8) An S corporation.''

SEC. 222. TREATMENT OF DISTRIBUTIONS DURING LOSS YEARS.

(a) ADJUSTMENTS FOR DISTRIBUTIONS TAKEN INTO ACCOUNT BEFORE LOSSES.—

(1) Subparagraph (A) of section 1366(d)(1) (relating to losses and deductions cannot exceed shareholder's basis in stock and debt) is amended by striking ''paragraph (1)'' and inserting ''paragraphs (1) and (2)(A)''.

(2) Subsection (d) of section 1368 (relating to certain adjustments taken into account) is amended by adding at the end the following new sentence:

''In the case of any distribution made during any taxable year, the adjusted basis of the stock shall be determined with regard to the adjustments provided in paragraph (1) of section 1367(a) for the taxable year.''

(b) ACCUMULATED ADJUSTMENTS ACCOUNT.—Paragraph (1) of section 1368(e) (relating to accumulated adjustments account) is amended by adding at the end the following new subparagraph:

''(C) NET LOSS FOR YEAR DISREGARDED.—

''(i) IN GENERAL.—In applying this section to distributions made during any taxable year, the amount in the accumulated adjustments account as of the close of such taxable year shall be determined without regard to any net negative adjustment for such taxable year.

''(ii) NET NEGATIVE ADJUSTMENT.—For purposes of clause (i), the term 'net negative adjustment' means, with respect to any taxable year, the excess (if any) of—

''(I) the reductions in the account for the taxable year (other than for distributions), over

''(II) the increases in such account for such taxable year.''

(c) CONFORMING AMENDMENTS.—Subparagraph (A) of section 1368(e)(1) is amended—

(1) by striking ''as provided in subparagraph (B)'' and inserting ''as otherwise provided in this paragraph'', and

(2) by striking ''section 1367(b)(2)(A)'' and inserting ''section 1367(a)(2)''.

SEC. 223. CONSENT DIVIDEND FOR AAA BYPASS ELECTION.

Section 1368(e)(3) (relating to election to distribute earnings first) is amended by adding at the end the following new subparagraph:

''(C) CONSENT DIVIDEND.—Under regulations prescribed by the Secretary, an S corporation may, subject to the election under this paragraph, consent to treat as a distribution the amount specified in such consent, to the extent such amount does not exceed the accumulated earnings and profits of such corporation. The amount so specified shall be considered—

''(i) as distributed in money by the corporation to its shareholders on the last day of the taxable year of the corporation and as contributed to the capital of the corporation by the shareholders on such day, and

''(ii) if any such shareholder is an organization described in section 511(a)(2), as unrelated business taxable income (as defined in section 512) to such shareholder.''

SEC. 224. TREATMENT OF S CORPORATIONS UNDER SUBCHAPTER C.

Subsection (a) of section 1371 (relating to application of subchapter C rules) is amended to read as follows:

''(a) APPLICATION OF SUBCHAPTER C RULES.—Except as otherwise provided in this title, and except to the extent inconsistent with this subchapter, subchapter C shall

apply to an S corporation and its shareholders.''

SEC. 225. ELIMINATION OF PRE-1983 EARNINGS AND PROFITS.

(a) IN GENERAL.—If—

(1) a corporation was an electing small business corporation under subchapter S of chapter 1 of the Internal Revenue Code of 1986 for any taxable year beginning before January 1, 1983, and

(2) such corporation is an S corporation under subchapter S of chapter 1 of such Code for its first taxable year beginning after December 31, 1995,

the amount of such corporation's accumulated earnings and profits (as of the beginning of such first taxable year) shall be reduced by an amount equal to the portion (if any) of such accumulated earnings and profits which were accumulated in any taxable year beginning before January 1, 1983, for which such corporation was an electing small business corporation under such subchapter S.

(b) CONFORMING AMENDMENTS.—

(1)(A) Subsection (a) of section 1375 is amended by striking ''subchapter C'' in paragraph (1) and inserting ''accumulated''.

(B) Subsection (b) of section 1375, as amended by section 214(c)(2), is amended by striking paragraph (3) and by redesignating paragraphs (4) and (5) as paragraphs (3) and (4), respectively.

(C) The section heading for section 1375 is amended by striking ''**subchapter c**'' and inserting ''**accumulated**''.

(D) The table of sections for part III of subchapter S of chapter 1 is amended by striking ''subchapter C'' in the item relating to section 1375 and inserting ''accumulated''.

(2) Clause (i) of section 1042(c)(4)(A), as amended by section 214(c)(5), is amended by striking ''section 1375(b)(5)'' and inserting ''section 1375(b)(4)''.

SEC. 226. ALLOWANCE OF CHARITABLE CONTRIBUTIONS OF INVENTORY AND SCIENTIFIC PROPERTY.

(a) IN GENERAL.—Section 170(e) (relating to certain contributions of ordinary income and capital gain property) is amended—

(1) by striking ''(other than a corporation which is an S corporation)'' in paragraph (3)(A), and

(2) by striking clause (i) of paragraph (4)(D) and by redesignating clauses (ii) and (iii) of such paragraph as clauses (i) and (ii), respectively.

(b) STOCK BASIS ADJUSTMENT.—Paragraph (1) of section 1367(a) (relating to adjustments to basis of stock of shareholders, etc.) is amended by striking ''and'' at the end of subparagraph (B), by striking the period at the end of subparagraph (C) and inserting '', and'', and by adding at the end the following new subparagraph:

''(D) the excess of the deductions for charitable contributions over the basis of the property contributed.''

SEC. 227. C CORPORATION RULES TO APPLY FOR FRINGE BENEFIT PURPOSES.

(a) IN GENERAL.—Section 1372 (relating to partnership rules to apply for fringe benefit purposes) is repealed.

(b) PARTNERSHIP RULES TO APPLY FOR HEALTH INSURANCE COSTS OF CERTAIN S CORPORATION SHAREHOLDERS.—Paragraph (5) of section 162(*l*) is amended to read as follows:

''(5) TREATMENT OF CERTAIN S CORPORATION SHAREHOLDERS.—

''(A) IN GENERAL.—This subsection shall apply in the case of any 2-percent shareholder of an S corporation, except that—

''(i) for purposes of this subsection, such shareholder's wages (as defined in section 3121) from the S corporation shall be treated as such shareholder's earned income (within the meaning of section 401(c)(1)), and

''(ii) there shall be such adjustments in the application of this subsection as the Secretary may by regulations prescribe.

''(B) 2-PERCENT SHAREHOLDER DEFINED.—For purposes of this paragraph, the term '2-percent shareholder' means any person who owns (or is considered as owning within the meaning of section 318) on any day during the taxable year of the S corporation more than 2 percent of the outstanding stock of such corporation or stock possessing more than 2 percent of the total combined voting power of all stock of such corporation.''

(b) CONFORMING AMENDMENT.—The table of sections for part III of subchapter S of chapter 1 is amended by striking the item relating to section 1372.

TITLE III—TAXATION OF S CORPORATION SHAREHOLDERS

SEC. 301. UNIFORM TREATMENT OF OWNER-EMPLOYEES UNDER PROHIBITED TRANSACTION RULES.

The last sentence of section 4975(d) (relating to exemptions from prohibited transactions) is amended by striking ''a shareholder-employee (as defined in section 1379, as in effect on the day before the date of the enactment of the Subchapter S Revision Act of 1982),''.

SEC. 302. TREATMENT OF LOSSES TO SHAREHOLDERS.

(a) TREATMENT OF LOSSES IN LIQUIDATIONS.—Section 331 (relating to gain or loss to shareholders in corporate liquidations) is amended by redesignating subsection (c) as subsection (d) and by inserting after subsection (b) the following new subsection:

''(c) LOSSES ON LIQUIDATIONS OF S CORPORATION.—

''(1) IN GENERAL.—The portion of any loss recognized by a shareholder of an S corporation (as defined in section 1361(a)(1)) on amounts received by such shareholder in a distribution in complete liquidation of such S corporation which does not exceed the ordinary income basis of stock of such S corporation in the hands of such shareholder shall not be treated as a loss from the sale or exchange of a capital asset but shall be treated as an ordinary loss.

''(2) ORDINARY INCOME BASIS.—For purposes of this subsection, the ordinary income basis of stock of an S corporation in the hands of a shareholder of such S corporation shall be an amount equal to the portion of such shareholder's basis in such stock which is equal to the aggregate increases in such basis under section 1367(a)(1) resulting from such shareholder's pro rata share of ordinary income of such S corporation attributable to the complete liquidation.''

(b) CARRYOVER OF DISALLOWED LOSSES AND DEDUCTIONS UNDER AT-RISK RULES ALLOWED.—Paragraph (3) of section 1366(d) (relating to carryover of disallowed losses and deductions to post-termination transition period) is amended by adding at the end the following new subparagraph:

''(D) AT-RISK LIMITATIONS.—To the extent that any increase in adjusted basis described in subparagraph (B) would have increased the shareholder's amount at risk under section 465 if such increase had occurred on the day preceding the commencement of the post-termination transition period, rules similar to the rules described in subparagraphs (A) through (C) shall apply to any losses disallowed by reason of section 465(a).''

TITLE IV—EFFECTIVE DATE

SEC. 401. EFFECTIVE DATE.

(a) IN GENERAL.—Except as otherwise provided in this Act, the amendments made by this Act shall apply to taxable years beginning after December 31, 1995.

(b) TREATMENT OF CERTAIN ELECTIONS UNDER PRIOR LAW.—For purposes of section 1362(g) of the Internal Revenue Code of 1986 (relating to election after termination), any termination under section 1362(d) of such Code (as in effect on the day before the date of the enactment of this Act) shall not be taken into account.

Mr. HATCH. Mr. President, I also want to pay specific tribute to our distinguished colleague from Arkansas, Senator PRYOR. Not only has he been a great Senator here but he has been the leader on this particular issue for years and he deserves the credit for these changes in the S corporation law. I have agreed to assistance this year in trying to get this done and we intend to get it done this year. It is something that is long overdue, and thanks to his leadership and his intellectual prowess I think we will be able to get it done. So I want to personally compliment him.

Mr. PRYOR. Mr. President, first I would like to thank my very good friend, my long-time friend and distinguished colleague from Utah, Senator HATCH.

Senator HATCH and I have worked on this proposal for a long time and we are very proud today to be able to introduce it as a bill and to also announce our 23 cosponsors from each side of the aisle in support of the S Corporation Reform Act of 1995.

Senator HATCH has been, certainly, a teacher for me in this whole process. I thank him. He has been a great ally. Truly, serving on the Finance Committee together, working with this legislation and working with a number of colleagues that we have in support, and also the number of organizations that I will list in a moment, we think truly in 1995 we can make this reform of S corporation law become a reality.

This legislation is truly the culmination of the efforts of many, many individuals and groups. It is a bipartisan effort, and certainly represents, I think, a step that Congress can and should take in order to capitalize on one of our country's most valuable resources, small business, as Senator HATCH has just so eloquently stated.

I want to thank all of the businessmen and women, attorneys, accountants, and small business organizations who have worked with me and my staff to help us to understand the unique problems of subchapter S corporations. They have helped us arrive at solutions that we think are easily administered and targeted to encourage economic growth.

The interest and enthusiasm for this effort is of special mention. At this date, the bill is endorsed by the :

Members of the S Corp Subcommittee of the American Bar Association's tax section; the U.S. Chamber of Commerce; National Federation of Independent Businesses Small Business Legislative Council; American Institute of Certified Public Accountants; American Vintners Association; American Consulting Engineers Council;

American Electronics Association; Associated Builders and Contractors; Associated Equipment Distributors; National Association of Life Underwriters; National Association of Realtors; National Association of Wholesale-Distributors; National Business Owners Association; National Society of Public Accountants; and the S Corp Reform Project.

Mr. President, these fine organizations we think represent hundreds of thousands of businesses across this country that will be impacted in a good way across our country. It is quite a team, and a team that I think is very rarely put together. It is quite a team that has worked thoughtfully and diligently, and I must say, patiently, through this system to help produce a bill that Congress can pass and we should pass overwhelmingly.

Mr. President, I would like to point out to my colleagues that I introduced similar legislation in the last session of Congress. On November 19, 1993, S. 1690 was introduced with our former colleague, Senator John Danforth, who retired from the U.S. Senate. Working together, we were joined by a strongly bipartisan group of 40 of our colleagues who cosponsored that bill at that time.

Today, once again, I am so proud to be able to join my friend and colleague, Senator HATCH, with whom I very much look forward to working in order that we might take the next step and move this bill into law.

The S Corporation Reform Act of 1995 contains 27 provisions designed to usher sub-S corporations into the financial environment of the 1990's.

Subchapter S was first enacted in 1958. In fact, I think it might have been about the year that the distinguished occupant of our chair was born. On that particular date that subchapter S was passed into law, it was enacted to remove tax considerations from small business owners' decisions to incorporate. This tax treatment has proved helpful to small business over the years, especially to startup businesses, to new businesses. But subchapter S, as originally enacted in 1958, was very limiting and contained a large number of pitfalls. Today, hundreds of thousands of U.S. businesses are S corporations. These businesses are still subject to many of the oppressive restraints which date back to its original enactment in 1958.

Mr. President, it goes without saying that times have changed a great deal since that year. The financial environment is far more complex than the 1950's. Sub S limitations restrict growth opportunities, and frankly sub S needs an overhaul, and it needs an overhaul now.

This legislation we think is the overhaul we need. It is an overhaul that is doable. It is an overhaul that can give a boost to our economic recovery by creating more opportunities for capital growth and jobs throughout every segment of American economic activity.

Mr. President, these objectives are met by this legislation in ways that have been carefully thought through. There may well be other ways to encourage these goals that Senator HATCH and I share this afternoon. But I hope and expect my colleagues respectfully will come forward with their ideas should they see areas where we might improve upon this proposal. I look forward to this dialog. I urge my colleagues to examine this bill closely and to join with Senator HATCH and myself in this effort.

Mr. President, I ask unanimous consent that a copy of a summary description of the major provisions of this bill be printed in the RECORD.

There being no objection, the material was ordered to be printed in the RECORD, as follows:

S CORPORATION REFORM ACT OF 1995

ACCELERATING CAPITAL FORMATION

Shareholder limitations

Increase the number of permitted shareholders from 35 to 50. Currently a corporation is not eligible to be an S corporation if it has more than 35 shareholders. Increasing the number of permitted shareholders to 50 will make S corporation status available to additional closely-held businesses, allowing them the benefits of limited liability. Further, increasing the number of permitted shareholders will enable S corporations to raise more capital.

Permit tax-exempt organizations to be shareholders. This would permit charities and pension plans to be eligible shareholders of an S corporation, thereby increasing an S corporation's access to certain capital markets. Specifically, an S corporation would be able to establish an employee stock ownership plan and would have access to additional capital from charitable organizations and pension funds. The bill further provides that the flow-through income of an S corporation would be treated as unrelated business taxable income to a tax-exempt shareholder as if the S corporation's activities were conducted directly by the tax-exempt shareholder.

Allow nonresident alien shareholders to own S corporation stock. By permitting nonresident aliens to be eligible shareholders of an S corporation, the bill expands an S corporation's access to capital. In addition, it enhances an S corporation's ability to expand into international markets because it provides them the ability to offer an equity interest to individuals they are trying to recruit to grow their business overseas. To ensure collection of tax on nonresident aliens, the bill subjects these shareholders to U.S. withholding tax on S corporation income.

Preferred Stock and Convertible Debt

Permit S corporations to issue preferred stock. Currently, S corporations may not issue more than one class of stock. By permitting S corporations to issue preferred stock, the bill increases access to capital from investors who insist on having a preferential return. The provision also facilitates family succession by permitting the older generation of shareholders to relinquish control of the corporation but maintain an equity interest. The bill also provides that a distribution made with respect to qualified preferred stock will be considered interest income to the shareholder and deductible interest expense to the S corp.

Expand Safe Harbor Debt to permit convertible debt. This provision permits S corporations to issue debt that may be converted into stock of the corporation provided that the terms of the debt are substantially the same as the terms that could have been obtained from an unrelated party. The provision will also permit the debt to be held not only by qualified shareholders, but also by a person who is actively and regularly engaged in the business of lending money. The current law provision, which prohibits conversion of the debt into stock, unnecessarily impairs the ability of an S corporation to raise investment capital.

Subsidiaries

Permit an S corporation to own greater that 80% of another corporation. Currently, S corporations may not own more than 79% of a C corporation. This provision removes this limitation to allow S corporations to hold more than 80% of the stock of a subsidiary C corporations, which will greatly enhance an S corporation's ability to achieve significant non-tax objectives in structuring their operations. In reality, taxpayers get around current rules through complex arrangements used by expensive tax planners. So, this provision allows S corporation to do directly, what they now do indirectly.

Permit S Corporations to own wholly-owned S Corporation Subsidiaries. The provision would permit an S corporation to serve as a holding company for the various operating S corporations, which would simplify management of the group. The holding company could enter into contracts on behalf of the group, serve as a common paymaster, perform other centralized management services, and facilitate obtaining financing for the group.

PRESERVING FAMILY-OWNED BUSINESSES

Expand the types of trusts that can own S corporation stock to include certain complex trusts that qualify as ''electing small business trusts.'' This provision would enable S corporation shareholders to accomplish many estate planning goals not currently available because of current law limitations on the types of trusts that can be S corporation shareholders. Specifically, this provision would enable S corporation shareholders to establish complex trusts with multiple beneficiaries and permit the trustee to have discretion as to which beneficiary to make distributions. Providing this type of flexibility is consistent with a major underlying purpose of the S corporation—to provide a vehicle for family-owned corporations.

Count all members of a single family that own an S corporation's stock as a single shareholder. An election could be made with the consent of all shareholders to count family members that are not more than six generations removed from a common ancestor as one shareholder for purposes of the number of shareholder limitation.

REMOVING TRAPS FOR THE UNWARY

Elections

Permit the Secretary of the Treasury to treat invalid elections as effective and permit late elections. This provision permits the IRS to retroactively validate an invalid S corporation election in cases where the corporation inadvertently failed to meet the definition of a small business corporation or to obtain the required shareholder consents. The bill sets forth the criteria under which the IRS should validate such elections. The bill also provides for an automatic waiver procedure for certain inadvertent terminations. In addition, the bill provides that if a corporation fails to make a timely S election (i.e., by the 15th day of the third month of the first S corporation year) and the Secretary determines that there was reasonable cause for the failure to make such election, the Secretary may treat the election as timely made.

Passive Investment Income

Repeal excessive passive income as a termination event. Under current law, if more than 25 percent of the gross receipts of an S corporation are passive investment income, a corporate level tax will be imposed on the excess passive income. In addition, en election of S corporation status will be terminated if at the close of three consecutive years a corporation has subchapter C earnings and profits and more than 25 percent of gross receipts are from passive investment income. The provision would increase the threshold for taxing excess passive income from 25 percent to 50 percent. Importantly, the provision would also provide that an S corporation would not lose its S corporation status if it has excess passive income for three consecutive years. Instead, the corporate level tax rate applied to the excess passive income would increase by 10 percent for each successive year. The provision also makes it clear that items of income connected with an S corp's trade or business will not be considered passive income.

FRINGE BENEFITS

Place S corporation shareholders in the same position as regular corporations with respect to fringe benefits such as life insurance premiums.

Repeal restrictions on qualified plan loans made to S corporation shareholders.

TECHNICAL PROPOSALS

Treat losses on liquidation of S corporations as ordinary to the extent the loss created by ordinary income passthrough triggered the liquidation. In the case of a liquidation of an S corporation, current law can result in double taxation because of a mismatch of ordinary income (realized at the corporate level and passed through to the shareholder) and a capital loss (recognized at the shareholder level on the liquidating distribution). Although careful tax planning can avoid this result, many S corporations do not have the benefit of sophisticated tax counsel. The provision in the bill would eliminate this potential trap.

Allow interim closing of the books in termination of shareholder interest with consent of corporation and affected shareholder. Current law requires that if a shareholder terminates his interest in an S corporation during the taxable year, the corporation and all persons who are shareholders during the taxable year must agree to close the books on the date of termination. The bill would eliminate the requirement that all shareholders consent to the closing and instead requires only that the ''affected shareholders'' (the shareholder whose interest is terminated and all shareholders to whom such shareholder transferred shares during the year) consent to the closing. This change will ease procedural problems in preparing and filing timely corporate tax returns.

Allow charitable contributions of inventory and scientific property to be the same for S corporations as for regular corporations. S corporations would be permitted an increased charitable contribution, equivalent to the deduction amount allowed to regular corporations.

By Mr. BRADLEY (for himself and Mr. HOLLINGS):

S. 759. A bill to amend the Immigration and Nationality Act to limit the adjustment of status of aliens who are unlawfully residing in the United States; to the Committee on the Judiciary.

THE ILLEGAL IMMIGRATION ENFORCEMENT ACT OF 1995

Mr. BRADLEY. Madam President, I am pleased to introduce, for myself and Senator HOLLINGS, the Illegal Immigration Enforcement Act of 1995. This is a bill to improve the Federal Government's ability to deter illegal immigration by enhancing enforcement of existing laws that prohibit employment of illegal aliens and bar overstays by legally admitted visitors.

Madam President, I have been watching the unfolding immigration debate with real concern. As I followed California's proposition 187 campaign, I realized the arguments over illegal immigration are occurring in a vacuum. We are trying to address the impact of immigration without understanding how it relates to the deeper transformations that are shaping our society. We find ourselves susceptible to the demagogic quick fix, and risk undermining the diversity that underlies our strength as an American people.

Peter Drucker once said:

Every few hundred years throughout Western history, a sharp transformation has occurred. In a matter of decades, society rearranges itself—its world view, its basic values; its social and political structures; its art; its key institutions. Fifty years later, there is a new world. And the people born into that world cannot even imagine the world in which their grandparents lived and into which their own parents were born.

Madam President, we are currently living through such a period of transformation. Not since the age of democratic revolution coincided with the industrial revolution has our world undergone such sweeping change as we are having today. The forces at work in our lives today are as dramatic and powerful as the Declaration of Independence and the steam engine were two centuries ago.

We face today a rapidly transforming world full of new opportunities. But those opportunities are accompanied by profound uncertainties and painful adaptations. Progress creates losers as well as winners. For example, the death of the Soviet Union has ended our fear of nuclear annihilation. At the same time, the resulting military downsizing has cost over 1.1 million jobs in the defense sector alone since 1987. As a result, and not for the first time in our history, politicians and voters have seized upon immigration, especially illegal immigration, as a scapegoat for the deeper uncertainties we feel.

Illegal immigration has also become a lightning rod for worries about the budget crises we face at all levels of Government. There is no doubt that illegal immigrants impose a cost on taxpayers. According to the estimates by the Urban Institute, the seven most affected States pay approximately $3.1 billion yearly on education, $471 million on incarceration, and $313 million on providing medical treatment for undocumented aliens. The Urban Institute's fiscal year 1993 estimates for my own State of New Jersey, which has the sixth largest population of illegal aliens, are $146 million for education, $6.6 million for incarceration, and $0.5–3.9 million for Medicaid, for a total of $153.1–156.5 million.

Anger over illegal immigration inevitably creates a backlash against legal immigrants and even citizens of different ethnic backgrounds. However, this is a self-defeating response. Our country is increasingly a mixture of races, languages, and religions, as new immigrants arrive in search of economic promise and political freedom. By the year 2000, only 57 percent of the people who enter the work force in America will be native-born white Americans. That means that the economic future of all Americans will depend increasingly on the talents of nonwhite Americans. We will all either advance together or each of us will be diminished.

We most need to appreciate the remarkable opportunity that our racial and ethnic diversity represents for the future of our country. Our immigrants and new citizens can be our guide to the cultural rhythms in the fastest growing areas of the world economy. Given high-quality and price-competitive goods, the cultural knowledge they have can American the advantage. Our diversity can mean more jobs, more prosperity for all Americans, if we can seize the moment and not run away from it.

To do so, we must reinvigorate the institutions and organizations which integrate new arrivals into American society. I have spoken elsewhere of the crisis afflicting civil society in this country. One of the effects of the decline of the institutions of civil society is the weakening of the lodges, clubs, churches, Scout troops, and other organizations which used to give immigrants entree into American society. As a result, we all too often see groups of teenage immigrants operating on the fringes of society instead of productive new members integrating into the heart of American society.

We cannot realize the opportunity presented by our diversity if we let frustration over the Federal Government's inability to control its borders spill over into action against those who are here legally. We must control illegal immigration in order to make our country safe for legal immigration. We must control illegal immigration if we are to make our country safe for diversity.

There is no shortage of laws on the books to control illegal immigration. There are laws to punish employers and smugglers of illegal aliens, to deny illegal aliens most Government benefits and even to compensate the States for some of the costs associated with illegal immigration.

The primary problem, however, is enforcement. The Immigration and Naturalization Service is underfunded and hindered by a history of incompetence that the current management is hard

put to reverse. The INS cannot keep illegal aliens out of the country, track them once they enter, or remove them once they are identified. Its various databases are, frankly, a shambles.

At the same time, certain economic interests benefit from the labor of illegal aliens. They profit from the general climate of neglect in which they can demand long hours of labor for low wages and few benefits.

Madam President, sweatshops manned by illegal men, women, and children are a disgrace to America and a drag on the fortunes of legal immigrant and American workers. These are the very inhumane labor conditions and practices we try to improve in countries abroad, but they are here, in America, today. American workers and honest American employers should not have to compete against this exploited labor force.

That brings me, Madam President, to my bill, the Illegal Immigration Enforcement Act of 1995. This legislation contains three major provisions which can help end this gentleman's agreement and will enforce the laws that are on the books. The gentleman's agreement is: pass tough legislation, but do not enforce it. Talk about being tough on illegal immigrants, but allow certain economic interests to benefit from illegal immigrant labor.

The first provision goes to, I think, the root problem, which is employment. Most illegal aliens do not come to the United States for health care or welfare or even education. They come to work. That means that the way to discourage them is not to punish their children by denying them medical care or education, as proposition 187 tries to do, but instead remove the employment magnet and remove the incentive that attracts them to the United States.

Existing law, starting with the Immigration Reform and Control Act of 1986, contains provisions which would reduce employment opportunities for illegal immigrants if they were simply enforced. Before enacting fundamental changes in this bedrock piece of legislation, we should try enforcing the laws already on the books. Empty legislating is no substitute for enforcement.

The place to start is employer sanctions. The 1986 act, better known as the Simpson-Mazzoli Act, imposes civil penalties on employers of illegal aliens of up to $10,000 per alien for repeat offenders. There is also a criminal penalty of up to 6 months imprisonment and a $3,000 fine for pattern or practice violations.

Madam President, enforcement of employer sanctions is a low priority at INS. In part, this is because the labor regulatory function is different from the policing function usually done by the investigative branch of the Immigration and Naturalization Service. As in any bureaucracy, ''different'' means ''low priority.''

In addition, this branch has a mandate to focus on antismuggling and removal of criminal aliens. By implication, everything else has low priority.

This low priority shows up in the figures. The 1986 act authorized $100 million per year to enforce employer sanctions, and even that was probably too little, but by fiscal year 1994, the appropriation had shrunk to $23 million. Funding has recovered somewhat since 1994, but remains well under the amount necessary to implement the law properly.

As a result, the number of cases investigated has declined by nearly 50 percent from 1989 to 1994. In particular, the number of investigations resulting from leads, the most productive investigations, declined from 5,118 in 1989 to 2,240 in 1994.

It is clear that as long as the same INS branch tries to perform investigative and employer sanctions functions, the latter will have to take a back seat. The way it is currently structured, employer sanctions will always take a back seat.

My bill fixes this problem by creating a separate Office for the Enforcement of Employer Sanctions and authorizing it for $100 million, the figure that was contained in the 1986 Act.

This first provision of my bill also addresses the potential for employment discrimination that exists in any employment eligibility legislation. For example, in 1990, a GAO study found that the 1986 act's employer sanctions provisions resulted in employment discrimination. The study suggested three causes for this:

First, the employers do not understand the law's requirements; second, employers do not understand how to determine employment eligibility; and third, the prevalence of counterfeit documents increases employer confusion.

As the GAO study implies, the problem is not with the law but with the INS's failure to educate employers about what the law requires them to do. Most employers, for example, still do not know that they must fill out an I–9 employment eligibility form for every employee, whether that employee is white, African-American, Hispanic, Asian, or otherwise. This is the key to combating discrimination, educating employers that this form applies to all.

Note that the GAO study reports that an estimated 346,000 employers said that they applied the 1986 act's verification system only to persons who had a foreign appearance or accent, and recommends, among other steps, increasing employer understanding through effective education efforts.

Madam President, my bill takes this problem head on by mandating that the INS Office for the Enforcement of Employer Sanctions be charged with ''educating employers on the requirements of the law, and in other ways as is necessary to prevent employment discrimination.''

The bottom line, then, is that my bill does not add to employers' burdens; it does not add one single form to the mountain of paperwork they must already fill out when they hire a new legal worker. Instead, it requires the Federal Government to explain the existing law to them. In this way, it will reduce the burden of uncertainty employers now bear.

Let me point out as well that the bill complements other efforts by the administration, Senator FEINSTEIN, Senator SIMPSON—the coauthor of the 1986 act—and others, to reduce the number of documents that can be used to confirm employment eligibility, make it more difficult to counterfeit the documents and develop a more reliable national employment eligibility data base.

So, Madam President, the first initiative in the bill is to tighten up employer sanctions.

Second, the bill prevents illegal aliens from reaping the rewards of their illegal entry into the United States. It prohibits adjustment of status within the United States for those seeking employment-based legal immigrant status. Further, it disqualifies those who have worked illegally in the United States from becoming legal immigrants. Currently, those in the United States illegally can try to adjust to a legal status, based upon family relationship or employment in a hard-to-fill job.

While I do not advocate separating families, we can and should go after those who come to the United States illegally and expect to find an employer who will sponsor them for adjustment to legal status.

My bill does this by forcing those who want to adjust for work-related reasons to do so outside the United States. So that, if they are denied, they cannot simply melt back into the population. In addition, by making previous illegal employment a disqualification for adjustment of status for work-related reasons, this bill denies illegal workers the benefit of their lawbreaking.

Finally, Madam President, the bill addresses the problem of overstays by visitors admitted to this country legally. The debate on illegal immigration is focused on the United States-Mexican border. This is understandable, given the flow of illegal aliens across the border and the impact of this flow on border States. However, even sealing off the United States-Mexican border would not solve the problem of illegal immigration.

Indeed, Madam President, the United States-Mexican border is less than half of the problem. The Immigration and Naturalization Service estimates that 52 percent of all illegal aliens residing in the United States do not sneak across the U.S. border. Instead, they enter legally on visitor's visas and then overstay their visas. The percentage in my State of New Jersey is even higher, given its distance from Mexico and the

sources of our illegal alien population. The INS estimates that 60 percent of New Jersey's illegal aliens enter the country legally on a visitor's visa and then just overstay, convinced that the INS will never find them. And most times they are right.

The administration and Congress, fixated on the Mexican border, are ignoring this very substantial problem. My bill addresses it by requiring the INS to develop an entry and exit data base that will alert it to overstays by legally admitted nonimmigrants. It is pretty simple. We cannot hope to control our borders unless we know who is inside them. Once we know who is overstaying his or her visa and where that person is staying, we can easily take steps to remove that person from our country. It is a very simple step. It is not taken today, so you have 52 percent of the people who come on legitimate visas disappearing into the society as a whole.

Madam President, the terrorist atrocity in Oklahoma City reminded us that we live in a dangerous world. Of course, non-Americans have no monopoly on terrorism. That is what Oklahoma City said as well. The evidence indicates that the Oklahoma City bombing was not perpetrated by an illegal alien. However, illegal aliens overstaying tourism visas have been implicated in terrorism in this country. For example, take Mohammad Salameh, who is accused of having rented the van used in the World Trade Center bombing. He was living in the United States illegally at the time of that crime. He entered this country legally, on a 6-month tourist visa, on February 17, 1988. And he still had not departed at the time the World Trade Center bombing on February 26, 1993—5 years later.

Under current procedures, the INS had no idea of Salameh's failure to depart or his whereabouts in the United States. Under this bill, the INS would have been alerted to Salameh's overstay and illegal residence in the United States nearly 4½ years before the crime.

So, Madam President, there you have it. Enforcement of employer sanctions, restrictions on rewarding aliens for illegal work, and measures to discourage overstays by legally admitted visitors. With these steps toward enforcing existing law, we can help to build common ground here at home, to parlay our diversity into strength, to protect legal immigration, and to lead the world by the power of our example.

Mr. President, I ask unanimous consent that the text of the bill be printed in the RECORD.

There being no objection, the bill was ordered to be printed in the RECORD, as follows:

S. 759

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the ''Illegal Immigration Enforcement Act of 1995''.

SEC. 2. FINDINGS.

The Congress makes the following findings:

(1) The Government of the United States has failed to curb the influx of undocumented aliens into the United States.

(2) The social and economic costs of illegal immigration create a backlash against legal immigrants and citizens of different ethnic backgrounds.

(3) The primary magnet for illegal aliens is work.

(4) Existing law contains provisions to prevent the employment of undocumented aliens.

(5) Properly enforced, these provisions could reduce employment opportunities for illegal immigrants and thereby reduce the incentive for illegal immigration.

(6) With proper enforcement and employer education, the employer sanctions laws should not result in employment discrimination.

(7) However, these laws are not now adequately enforced.

(8) This is in part because Immigration and Naturalization Service inspectors have other, legislatively mandated, priorities that have first call on their limited resources.

(9) Many illegal immigrants adjust their status to become legal residents.

(10) This prospect is another encouragement to illegal immigration.

(11) Statistics show that approximately one-half of all illegal aliens living in the United States arrived legally on nonimmigrant visas, then failed to depart.

(12) The Immigration and Naturalization Service (INS) is currently unable to identify or locate such visa overstayers in a systematic fashion.

SEC. 3. ENFORCEMENT OF EMPLOYER SANCTIONS.

(a) ESTABLISHMENT OF NEW OFFICE.—There shall be in the Immigration and Naturalization Service of the Department of Justice an Office for the Enforcement of Employer Sanctions (in this section referred to as the ''Office'').

(b) FUNCTIONS.—The functions of the Office established under subsection (a) shall be—

(1) to investigate and prosecute violations of section 274A(a) of the Immigration and Nationality Act (8 U.S.C. 1324a(a)); and

(2) to educate employers on the requirements of the law and in other ways as necessary to prevent employment discrimination.

(c) AUTHORIZATION OF APPROPRIATIONS.—There are authorized to be appropriated to the Attorney General $100,000,000 to carry out the functions of the Office established under subsection (a).

SEC. 4. LIMITATION ON ADJUSTMENT OF STATUS.

Section 245(c) of the Immigration and Nationality Act (8 U.S.C. 1255(c)) is amended—

(1) by striking ''or (4)'' and inserting ''(4)''; and

(2) by inserting before the period at the end the following: ''(5) any alien who seeks adjustment of status as an employment-based immigrant; or (6) any alien who was employed while the alien was an unauthorized alien, as defined in section 274(h)(3)''.

SEC. 5. MONITORING OF OVERSTAYS.

The Attorney General shall develop an entry and exit data base that will permit the Attorney General to identify lawfully admitted nonimmigrants who overstay their visas.

By Mr. ROCKEFELLER:

S. 760. A bill to establish the National Commission on the Long-Term Solvency of the Medicare Program; to the Committee on Finance.

THE MEDICARE COMMISSION ACT OF 1995

● Mr. ROCKEFELLER. Mr. President, I ask unanimous consent that the text of the bill be printed in the RECORD.

There being no objection, the bill was ordered to be printed in the RECORD, as follows:

S. 760

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the ''Medicare Commission Act of 1995''.

SEC. 2. ESTABLISHMENT.

(a) ESTABLISHMENT.—There is established a commission to be known as the National Commission on the Long-Term Solvency of the Medicare Program (hereafter in this Act referred to as the ''Commission'').

(b) MEMBERSHIP.—The Commission shall be composed of 15 members appointed as follows:

(1) Five members shall be appointed by the President from among officers or employees of the executive branch, private citizens of the United States, or both. Not more than 3 members selected by the President shall be members of the same political party.

(2) Five members shall be appointed by the Majority Leader of the Senate from among members of the Senate, private citizens of the United States, or both. Not more than 3 of the members selected by the Majority Leader shall be members of the same political party.

(3) Five members shall be appointed by the Speaker of the House of Representatives from among members of the House of Representatives, private citizens of the United States, or both. Not more than 3 of the members selected by the Speaker shall be members of the same political party.

(4) DATE.—The appointments of the members of the Commission shall be made no later than November 30, 1995.

(c) PERIOD OF APPOINTMENT; VACANCIES.—Members shall be appointed for the life of the Commission. Any vacancy in the Commission shall not affect its powers, but shall be filled in the same manner as the original appointment.

(d) INITIAL MEETING.—No later than 30 days after the date on which all members of the Commission have been appointed, the Commission shall hold its first meeting.

(e) MEETINGS.—The Commission shall meet at the call of the Chairman.

(f) QUORUM.—A majority of the members of the Commission shall constitute a quorum, but a lesser number of members may hold hearings.

(g) CHAIRMAN.—The Commission shall select a Chairman from among its members.

SEC. 3. DUTIES OF THE COMMISSION.

(a) ANALYSES AND RECOMMENDATIONS.—

(1) IN GENERAL.—The Commission shall—

(A) review relevant analyses of the current and long-term financial condition of the medicare trust funds;

(B) identify problems that may threaten the long-term solvency of such trust funds;

(C) analyze potential solutions to such problems that will both assure the financial integrity of the medicare program under title XVIII of the Social Security Act (42 U.S.C. 1395 et seq.) and the provision of appropriate health benefits; and

(D) provide appropriate recommendations to the Secretary of Health and Human Services, the President, and the Congress.

(2) DEFINITION OF MEDICARE TRUST FUNDS.—For purposes of this subsection, the term ''medicare trust funds'' means the Federal Hospital Insurance Trust Fund established under section 1817 of the Social Security Act

(42 U.S.C. 1395i) and the Federal Supplementary Medical Insurance Trust Fund established under section 1841 of such Act (42 U.S.C. 1395t).

(b) REPORT.—The Commission shall submit its report to the President and the Congress not later than December 31, 1996.

SEC. 4. POWERS OF THE COMMISSION.

(a) HEARINGS.—The Commission may hold such hearings, sit and act at such times and places, take such testimony, and receive such evidence as the Commission considers advisable to carry out the purposes of this Act.

(b) INFORMATION FROM FEDERAL AGENCIES.—The Commission may secure directly from any Federal department or agency such information as the Commission considers necessary to carry out the provisions of this Act. Upon request of the Chairman of the Commission, the head of such department or agency shall furnish such information to the Commission.

(c) POSTAL SERVICES.—The Commission may use the United States mails in the same manner and under the same conditions as other departments and agencies of the Federal Government.

SEC. 5. COMMISSION PERSONNEL MATTERS.

(a) COMPENSATION OF MEMBERS.—

(1) OFFICERS AND EMPLOYEES OF THE FEDERAL GOVERNMENT.—All members of the Commission who are officers or employees of the Federal Government shall serve without compensation in addition to that received for their services as officers or employees of the United States.

(2) PRIVATE CITIZENS OF THE UNITED STATES.—

(A) IN GENERAL.—Subject to subparagraph (B), all members of the Commission who are not officers or employees of the Federal Government shall serve without compensation for their work on the Commission.

(B) TRAVEL EXPENSES.—The members of the Commission who are not officers or employees of the Federal Government shall be allowed travel expenses, including per diem in lieu of subsistence, at rates authorized for employees of agencies under subchapter I of chapter 57 of title 5, United States Code, while away from their homes or regular places of business in the performance of services for the Commission, to the extent funds are available therefor.

(b) STAFF.—

(1) IN GENERAL.—The Chairman of the Commission may, without regard to the civil service laws and regulations, appoint and terminate an executive director and such other additional personnel as may be necessary to enable the Commission to perform its duties. At the request of the Chairman, the Secretary of Health and Human Services shall provide the Commission with any necessary administrative and support services. The employment of an executive director shall be subject to confirmation by the Commission.

(2) COMPENSATION.—The Chairman of the Commission may fix the compensation of the executive director and other personnel without regard to the provisions of chapter 51 and subchapter III of chapter 53 of title 5, United States Code, relating to classification of positions and General Schedule pay rates, except that the rate of pay for the executive director and other personnel may not exceed the rate payable for level V of the Executive Schedule under section 5316 of such title.

(c) DETAIL OF GOVERNMENT EMPLOYEES.—Any Federal Government employee may be detailed to the Commission without reimbursement, and such detail shall be without interruption or loss of civil service status or privilege.

(d) PROCUREMENT OF TEMPORARY AND INTERMITTENT SERVICES.—The Chairman of the Commission may procure temporary and intermittent services under section 3109(b) of title 5, United States Code, at rates for individuals which do not exceed the daily equivalent of the annual rate of basic pay prescribed for level V of the Executive Schedule under section 5316 of such title.

SEC. 6. TERMINATION OF THE COMMISSION.

The Commission shall terminate 30 days after the date on which the Commission submits its report under section 2(b).

SEC. 7. FUNDING FOR THE COMMISSION.

Any expenses of the Commission shall be paid from such funds as may be otherwise available to the Secretary of Health and Human Services.●

ADDITIONAL COSPONSORS

S. 216

At the request of Mr. HATCH, the name of the Senator from New York [Mr. D'AMATO] was added as a cosponsor of S. 216, a bill to repeal the reduction in the deductible portion of expenses for business meals and entertainment.

S. 230

At the request of Mr. DOLE, the name of the Senator from Maryland [Mr. SARBANES] was added as a cosponsor of S. 230, a bill to prohibit U.S. assistance to countries that prohibit or restrict the transport of delivery of U.S. humanitarian assistance.

S. 327

At the request of Mr. HATCH, the name of the Senator from New York [Mr. D'AMATO] was added as a cosponsor of S. 237, a bill to amend the Internal Revenue Code of 1986 to provide clarification for the deductibility of expenses incurred by a taxpayer in connection with the business use of the home.

S. 457

At the request of Mr. SIMON, the name of the Senator from Delaware [Mr. BIDEN] was added as a cosponsor of S. 457, a bill to amend the Immigration and Nationality Act to update references in the classification of children for purposes of U.S. immigration laws.

S. 471

At the request of Mr. BIDEN, the name of the Senator from Nevada [Mr. REID] was added as a cosponsor of S. 471, a bill to provide for the payment to States of plot allowances for certain veterans eligible for burial in a national cemetery who are buried in cemeteries of such States.

S. 506

At the request of Mr. CRAIG, the name of the Senator from Mississippi [Mr. LOTT] was added as a cosponsor of S. 506, a bill to amend the general mining laws to provide a reasonable royalty from mineral activities on Federal lands, to specify reclamation requirements for mineral activities on Federal lands, to create a State program for the reclamation of abandoned hard rock mining sites on Federal lands, and for other purposes.

S. 515

At the request of Mr. BRADLEY, the name of the Senator from Vermont [Mr. LEAHY] was added as a cosponsor of S. 515, a bill to amend the Federal Meat Inspection Act and the Poultry Products Inspection Act to provide for improved public health and food safety through the reduction of harmful substances in meat and poultry that present a threat to public health, and for other purposes.

S. 548

At the request of Mr. ROCKEFELLER, the name of the Senator from North Dakota [Mr. DORGAN] was added as a cosponsor of S. 548, a bill to provide quality standards for mammograms performed by the Department of Veterans Affairs.

S. 553

At the request of Mr. MOSELEY-BRAUN, the name of the Senator from Rhode Island [Mr. CHAFEE] was added as a cosponsor of S. 553, a bill to amend the Age Discrimination in Employment Act of 1967 to reinstate an exemption for certain bona fide hiring and retirement plans applicable to State and local firefighters and law enforcement officers, and for other purposes.

S. 580

At the request of Mrs. FEINSTEIN, the name of the Senator from California [Mrs. BOXER] was added as a cosponsor of S. 580, a bill to amend the Immigration and Nationality Act to control illegal immigration to the United States, reduce incentives for illegal immigration, reform asylum procedures, strengthen criminal penalties for the smuggling of aliens, and reform other procedures.

S. 641

At the request of Mrs. KASSEBAUM, the name of the Senator from Idaho [Mr. KEMPTHORNE] was added as a cosponsor of S. 641, a bill to reauthorize the Ryan White CARE Act of 1990, and for other purposes.

S. 650

At the request of Mr. SHELBY, the name of the Senator from Alabama [Mr. HEFLIN] was added as a cosponsor of S. 650, a bill to increase the amount of credit available to fuel local, regional, and national economic growth by reducing the regulatory burden imposed upon financial institutions, and for other purposes.

S. 733

At the request of Mr. ROTH, the name of the Senator from Massachusetts [Mr. KERRY] was added as a cosponsor of S. 733, a bill to amend title 23, United States Code, to permit States to use Federal highway funds for capital improvements to, and operating support for, intercity passenger rail service, and for other purposes.

S. 751

At the request of Mr. EXON, the name of the Senator from Nebraska [Mr. KERREY] was added as a cosponsor of S. 751, a bill to provide that certain games of chance conducted by a nonprofit organization not be treated as an unrelated business of such organization.